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C O N F I D E N T I A L SECTION 01 OF 02 ABUJA 002511

SIPDIS

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TAGS: PGOV ECON EPET EFIN
SUBJECT: OBASANJO TO RELEASE 1.2 BILLION EXCESS CRUDE REVENUE

REF: (A) ABUJA 2301 (B) LAGOS 2367 (C) ABUJA 997

Classified by Ambassador Howard F. Jeter for reasons 1.5 (b) and (d).

¶1. (C) Summary: During a September 26 Council of State meeting, President Obasanjo and state governors resolved their highly publicized squabble over the fate of excess oil revenues. In exchange for the governors accepting a partial allocation of 1.2 billion USD, Obasanjo agreed to eliminate the Federal Wage and Salary Commission and the Pensions Board. These bodies had previously affected state budgets, without the states' consent or input. The President signalled this compromise in a September 18 letter to IMF Managing Director Schroeder, arguing that political exigencies in Nigeria required a limited disbursal of excess revenues. In the same letter he urged the IMF not to allow the SBA to lapse in October. Obasanjo grappled with this Gordian knot as best he could. While the compromise makes an extension of the SBA more complicated, it may be the best deal Obasanjo could obtain politically: the governors had both the Constitution and much political weight on their side. End Summary.

Background

¶2. (SBU) Conflict between governors and the President over excess oil revenue has heightened political tensions in Abuja during the past six weeks. The arcane revenue flow procedure in Nigeria subject oil and non-oil revenues to a series of "first deductions" before being deposited into the Federation Account. Once in the account, this money is disbursed monthly according to a preset formula: 48.5% to the Federal Government, 24% to the states, 20% to local governments, and 7.5% to a special funds account controlled by the FG. If revenues after first line charges exceed the projected budgetary outlays for that month, the money is put into the Excess Revenue and Set Asides Account. (Ref C provides more detail on how the Federation Account is funded and its funds disbursed.) In determining the overall amount of the 2001 federal budget, planners used a 22 USD per barrel oil price, with a set production estimate that has proven to be overly-optimistic. Revenues exceeding 22 USD per barrel would then accrue to the Excess Proceeds Account. Based on actual production figures, excess revenue only accrues when the oil price exceeds 25.5 USD per barrel--the rest is consumed by planned 2001 spending.

¶3. (U) It is unclear what percentage of total annual excess proceeds the 1.2 billion USD represents. This amount will likely comprise the lion's share of excess proceeds for the year, given the recent drop in crude oil price below 25.5 USD per barrel. Obasanjo had blocked the transfer of excess proceeds funds to the Federation Account since concluding the current SBA with the IMF in August 2000.

¶4. (C) Economic arguments against releasing excess proceeds were substantial. The IMF, World Bank, and G-7 governments had pressured President Obasanjo to restrain spending in order to stabilize exchange and interest rates, to improve the macro-economic environment, and to build forex reserves. With the advent of value-for-money audits and budgetary due process procedure on federal capital expenditures, the IMF feels wasteful FG capital projects can be curtailed. The IMF opposes further dollops to state and local governments, not only based on monetary policy, but also because effective controls to prevent wasteful spending are lacking at the state level. Profligate spending at the state and local levels would only undermine efforts to enhance FG fiscal discipline, and would have a minatory effect on inflation and the value of the naira. (While some governors and LGA chairmen are behaving responsibly with their revenue, the majority are not.)

¶5. (C) The governors correctly asserted the Constitution

does not provide for special accounts outside of normal budgetary mechanisms. The Constitution states that all revenue must go into the Federation Account to be divided among federal, state and local governments. The governors also argued that the FG had been the most spend-thrift of all levels of government and that they should not be penalized for the toll the FG's intemperance has taken on the national economy. They point out that by creating discrete pots of money, the President creates an environment that promotes financial shenanigans. Many foresee a large FG political slush-fund for 2003, and are concerned that money will continue to be "re-allocated."

¶5. (C) Governors are also upset by what they see as unfunded mandates from Abuja that have a dramatic affect on their budgets but are established without consulting the state capitals. The new federal minimum wage and pension schemes being their most compelling examples. (COMMENT: Some governors have used their revenues wisely and responsibly. Foremost among these in the North would be Makarfi (Kaduna), Aleiro (Kebbi), Bafarawa (Sokoto) and Yar'Adua (Katsina). Peter Odili (Rivers) and Orji Kalu (Abia) are southern governors who appear to be making good use of their resources. James Ibori of Delta State has embarked on numerous costly building projects (such as office blocks and stadiums), and there is no reason to think Delta's contracting mechanisms are more transparent than those of the FG; on the contrary, newspapers recently carried dozens of full-page birthday wishes for Ibori -- paid by contractors and Delta officials currying favor. Meanwhile, Abubakar Audu of Kogi State recently purchased a home in Potomac, Maryland, for over $1.6 million with funds of unknown provenance; Poster-boy for Sharia' implementation Ahmed Sani Yerima of Zamfara State apparently cannot account for much of the money that has passed through his hands (septel). Circumstances are still worse at the local government level; observers agree that the vast majority of local governments exist primarily to divert revenue into the hands of government officials and their cronies. END COMMENT.)

Politics

¶6. (SBU) Advocates on both sides of this dispute--the Governors and the IMF--have bent the President's ear. Obasanjo, of course, was not a disinterested arbiter. Because of their evolution into an important independent political force, the governors will be major power-brokers in the 2003 election. For many governors, the conflict over excess crude proceeds has created more of a rift with the President than any other issue. It was a rift Obasanjo had to close. On the other hand, he had to tread lightly with the IMF for fear of jeopardizing the SBA, and the interest moratorium agreed to by the Paris Club.

¶7. (SBU) Due to this conundrum, President Obasanjo vacillated between hard-line no (August) to yes (early September) to "no more" (mid-September) to splitting the difference at the September 26 Council of State meeting. Acting as the governors' spokesman during the meeting, Governor Makarfi proposed the accepted compromise: if the FG would abolish several national commissions that regulate wages, pensions and employment, (no more unfunded mandates from Abuja), the governors would accept distribution of excess proceeds accruing during the first half of the year, along with a promise that GSM and privatization money will be placed in the Federation Account in due course. Makarfi believes the issue has been resolved, with everyone partly satisfied except perhaps the IMF.

¶8. (SBU) Comment: This compromise may have been the best deal Obasanjo could achieve politically while also trying to restrain spending to the extent possible. Much money will go to waste, and the concomitant influx of liquidity in the economy likely will push inflation higher and the naira lower. That said, some governors are delivering tangible benefits to their people, without borrowing against future revenue, and this money will allow them to continue to do so. As is so often the case here, the matrix of competing interests has led to slowly-evolved yet imperfect solutions that may be politically expedient but of questionable economic value. End Comment.
Jeter